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In the Supreme Court of the United States

OCTOBER TERM, 1972

No. 71-991

OTTER TAIL POWER COMPANY,
Appellant

v.

UNITED STATES OF AMERICA,
Appellee.

On Appeal From The United States District Court
For the District of Minnesota

Reply Brief for Amici Curiae

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The defect of the lower court's opinion is its mechanical application of antitrust rules without weighing their economic and regulatory implications.

The brief for the Government in this Court compounds the error by failing to face the problem of harmonizing legal precepts for the utility industry with its special economic and regulatory characteristics.

To fill this gap in the Government's brief, these *amici curiae** file this Reply Brief.

* General Public Utilities Corporation, Pacific Gas and Electric Company, San Diego Gas & Electric Company and Virginia Electric and Power Company.

SUMMARY OF ARGUMENT

The fundamental error of the lower court in this case was its misunderstanding of the nature of the electric utility industry. This case involves a public utility, not merely a regulated company. As compared with other regulated companies, a public utility is uniquely characterized by special economic circumstances and generally pervasive regulation, as the Court suggested in *United States* v. *Philadelphia Nat'l Bank*, 374 U.S. 321 (1963) at 352.

Antitrust rules derived in the unregulated industry context may be inapplicable for jurisdictional reasons when tested in a regulated industry, as appellant Otter Tail Power Co. ("Otter Tail") and amicus Federal Power Commission have demonstrated. We urge in addition that, even if applicable, the antitrust laws can be applied only in light of the specialized nature of public utility regulation, its purposes and effects. It follows that the lower court's use of per se analysis was in error and its conclusion of antitrust violation, unfounded.

The decision in this novel case, unless suitably restricted, may set the antitrust guidelines for an entire public utility industry. This Court should avoid an affirmance of the result below, which would preserve the mistaken judgment in this case and might mandate its application to the industry as a whole.

A. The Opinion Below Errs In Applying Per Se Antitrust Analysis

Otter Tail was charged with monopolization and attempted monopolization under section 2 of the Sherman Act by the refusal to sell electric power at wholesale, the refusal to wheel electric power to municipalities and the institution of litigation, all with the purpose and effect of foreclosing competition. Rather than evaluating the facts of the case in the light of the unusual economic characteristics of the electric utility industry and the fact of regulation, the lower court adopts the crude tools of per se categorization.

For instance, both lower court and Government conclude that Otter Tail possesses monopoly power in the retail market on the basis of mechanical application of market share standards. But this shows no recognition of the fact that the natural monopoly characteristics of the market may make such an effect inevitable, and the existence of economies of scale and the traditional policy against facility duplication may make such an effect desirable.

Once monopoly is established, court and Government proceed to the conclusion that any action taken to maintain such monopoly is unlawful. But the concept of public utility responsibility, which is the legally imposed obligation of regulated monopoly, requires just the kinds of actions that are described in antitrust vocabulary by the lower court as the unlawful maintenance of monopoly.

The uncritical application of antitrust precedent characterizes the treatment by the lower court and the Government of Otter Tail's refusals to sell power at wholesale and to wheel power for its former municipal customers. The lower court's reliance upon Otter Tail's alleged dominance of sub-transmission facilities can only be described as a misapplication of the "bottleneck theory" of antitrust law. No analysis whether in fact Otter Tail's facilities are necessarily a physical and economic bottleneck is undertaken. No recognition of the Federal Power Commission's authority to order interconnection, as it now has done in this case, is manifested.

The lower court and the Government make short shrift of Otter Tail's contention that its refusals were motivated by a desire to remain in business. Utilizing precedent from unregulated industries without natural monopoly characteristics, the lower court applied conventional antitrust reasoning in circular fashion to avoid the Otter Tail contentions. The Government acknowledges (Br. 91) that a refusal to deal does not necessarily violate the antitrust laws, even when engaged in by a monopolist. Yet not for a moment did the

lower court or the Government realize that Otter Tail was raising the real possibility that because of the peculiar nature of competition between private regulated monopoly and public unregulated monopoly, a requirement that Otter Tail make its capital facilities available to those seeking to avoid their own investment in bulk power supply would inevitably result in the disappearance of Otter Tail's retail market. The lower court ignored the question whether antitrust prefers, not competition over monopoly, but unregulated monopoly, after temporary competition, over regulated monopoly. In thus dismissing a serious contention, the lower court ignored an economic issue that may determine the industry's future structure.

Thus, the approach of the lower court, adopted by the Government, is per se categorization. The crucial fact of regulation and its effects is forgotten by the lower court and misunderstood by the Government. The policies that Federal and State governments have sought to effectuate through the regulatory scheme, and the implications those policies may have for antitrust application, are ignored. Both court and prosecutor avoid inquiry into the realities of competition. Oblivious to the economic effects of the actions it mandates, the lower court imposes per se concepts, devised for unregulated industry, without any thought of the confusion, conflict or disruption that will result in this industry. The Government does nothing to alleviate this mischief, but rather invites this Court's participation in it.

B. Applicable Precedent Prescribes Use of the Rule of Reason Antitrust Analysis

Instead of the rigid application of per se terminology, the lower court should have analyzed the facts of the case and evaluated the manner in which antitrust applied. Any such inquiry would have required the balancing of many factors, including the reasonableness of particular Otter Tail actions, competing public policies and the implications of intricate economic issues. In short, the antitrust

laws, if applicable at all, should have been applied in light of the rule of reason. Antitrust precedent provides authority for such a mode of analysis in this case.

After the enactment of the Sherman Act in 1890, it became apparent that its implementation depended upon some standard of reasonableness. In an early landmark case, *Standard Oil Co.* v. *United States,* 221 U.S. 1, 62 (1911), the Supreme Court, referring to section 2 of the Act condemning monopolization and conspiracy or attempts to monopolize, stated:

> "... [I]t becomes obvious that the criteria to be resorted to in any given case for the purpose of ascertaining whether violations of the section have been committed, is the rule of reason guided by the established law and by the plain duty to enforce the prohibitions of the act and thus the public policy which its restrictions were augustly enacted to subserve."

That concept of the Sherman Act's application has repeatedly been reaffirmed by this Court. For instance, in *United States* v. *Columbia Steel Co.,* 334 U.S. 495, 522, *n.* 19 (1948), the Court stated:

> "The general language of Sections 1 and 2 of the Sherman Act has been construed as prohibiting only unreasonable restraints, not all possible restraints of trade...."

The application of the rule of reason is especially appropriate in cases involving legal monopoly. In *United States* v. *United States Gypsum Co.,* 333 U.S. 364 (1948), the Court expressly applied the rule of reason to efforts to monopolize through use of patents. The same analysis should be valid in cases dealing with monopoly entrusted to an electric utility by government policy or devolving upon the same utility by the operation of economic forces in a natural monopoly market.

Furthermore, when the regulated sector of the economy is subjected to antitrust analysis, the precedents are likewise

clear that antitrust must be applied in full awareness of the peculiar facts of the individual case, taking into account the implications of regulation and the policy thereby sought to be effectuated.

> "Prohibitory legislation like the Sherman Law [*sic*], defining the area within which 'competition' may have full play, of course loses its effectiveness as the practical limitations increase; as such considerations severely limit the number of separate enterprises that can efficiently, or conveniently, exist, the need for careful qualification of the scope of competition becomes manifest. Surely it cannot be said in these situations that competition is of itself a national policy. To do so would disregard . . . those areas, loosely spoken of as natural monopolies or—more broadly—public utilities, in which active regulation has been found necessary to compensate for the inability of competition to provide adequate regulation." *Federal Communications Commission* v. *RCA Communications, Inc.*, 346 U.S. 86, 92 (1953).

Silver v. *New York Stock Exchange*, 373 U.S. 341 (1963), represents the Court's most complete discussion of the application of the antitrust laws in an industry subject to competing public policy articulated by federal statute. Conceding that the concerted refusal to deal there in issue would have been per se unlawful in the conventional industrial context, nevertheless the Court announced that the finding of such conduct,

> "[in] the presence of another statutory scheme, that of the Securities Exchange Act of 1934, means that such a conclusion is only the beginning, not the end, of inquiry." (At 349.)

What was required in that case, and should have been undertaken in this, was the reconciliation of antitrust and its policy of eliminating competitive restraints with the effectuation of competing public policy. This could only be done, in the words of the Court, by taking the fact of regulation into account:

> "But, under the aegis of the rule of reason, traditional antitrust concepts are flexible enough to permit the Exchange sufficient breathing space within which to carry out the mandate of the Securities Exchange Act." (At 360.)

The Court chose not to emphasize one public policy scheme over another, but rather to set up a "balance wheel" to enable the industry to operate

> "in a setting compatible with the objectives of both the antitrust laws and the Securities Exchange Act." (At 367.)

Thus, there is nothing in the antitrust laws requiring blind application of per se concepts in every case. Precedents authorize recourse to the standards of reasonableness to avoid arbitrary results. Particularly in the regulated industry context, factors in addition to the policy of preserving and enhancing competition must be considered. This the court below did not do, and for this reason its conclusion is fatally defective.

The "rule of reason" approach to this case would examine at least the nature of the particular industry involved, the economics of the industry, the facts and purposes of regulation and finally, the facts of the particular case. By ignoring three of these four central factors, the lower court distorted the analysis and made impossible a viable policy resolution of the controversy before it.

The electric utility industry is different from any other. Many of those differences have implications for antitrust. For instance, the public service obligation requires utilities to serve, and, as a consequence, to make provision for future demand. To construe such actions as the unlawful maintenance of monopoly is to impose contradictory legal standards. In addition, the crucial role of the industry in the economy of the country and the likelihood of extraordinary demand growth do suggest that antitrust policies be applied carefully and not dogmatically. Both the Govern-

ment and the opinion of the lower court miss these points.

Because it is the purpose of the antitrust laws to preserve and enhance competition, where that produces beneficial economic and social results, the lower court should have examined whether the results of its decision in this industry and in this case were in fact beneficial. Where there are grounds for believing the conventional laws of competition may not apply, or may apply differently, antitrust application ought to evaluate those grounds of belief. In addition, there is no effort, either in the opinion below or in the Government's brief, to address the implications of capital intensity within the industry, substantial economies of scale and resulting natural monopoly characteristics in industry markets, or even the presumed wastefulness of competition within the industry.

Even if no other factor were to be taken into account, the opinion below might have avoided confusion and possible public mischief by considering the fact of regulation designed to effectuate specific public policies. The policy purposes of regulation are to a great extent parallel to or identical with those of antitrust. When monopoly is regulated, the abuses proscribed by the antitrust laws are already denied to the monopolist. Where regulation can order access to a scarce resource, as the Federal Power Commission has now done in this case, the antitrust laws may have no part to play. The point is—a point ignored by both Government and lower court—that the policy interaction between regulatory agencies and antitrust enforcement is a fact of central importance in the industry and in this case.

The exaltation of one policy at the expense of all others makes little economic or legal sense. In this case, precedent prescribes that the antitrust law be applied only after weighing and evaluating competing public policies and the implications such policies have for this particular industry. Antitrust is not weakened but applied with due regard to the need to effectuate the policy of regulation. But by the

same reasoning, regulatory and competing public policies are not to be presumed to have been repealed by antitrust.

This is precisely the issue raised by this case. By ignoring this issue, the Government seeks to obtain results that may be applied, equally blindly, in case after case across the length and breadth of this industry. Before the Court lends itself to that effort, it should be confident that the lower court has considered all the relevant factors. This the lower court failed to do and accordingly, it should be reversed.

Respectfully submitted,

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